Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C.

In the Matter of Request for Extension of the Sunset Date of the Structural, Non-Discrimination, and Other Behavioral Safeguards Governing Bell Operating Company Provision of In-Region, Inter-LATA Information Services	CC Docket No. 96-149

Reply Comments of the Information Technology Association of America

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SUMMARY

The four surviving Bell Operating Companies ("BOCs") have filed strongly worded oppositions to the CIX/ITAA request to extend, until February 8, 2002, the sunset date for the safeguards governing BOC participation in the inter-LATA information services. The BOCs' arguments, however, are not persuasive.

The BOCs Have Distorted the Regime Adopted by Congress

The BOCs have distorted the BOC entry regime that Congress crafted – which sought to allow the BOCs to enter the inter-LATA telecommunications and information services markets, while imposing a comprehensive set of safeguards designed to prevent anti-competitive abuse.

Congress intended the safeguards to govern BOC entry into the inter-LATA markets. The BOCs argue that, while Congress created a comprehensive safeguards regime, and expressly made these safeguards applicable to BOC provision of both inter-LATA telecommunications and information services, Congress did not care whether this regime sunsets before *ever* being applied to BOC provision of information services. This is plainly incorrect.

Although Congress did not explain why it selected the February 8, 2000 as the presumptive sunset date for application of the safeguards to BOC provision of inter-LATA information services, the most plausible explanation is Congress assumed that most (if not all) of the BOCs would rapidly open their local markets to competition. Had they done so, the BOCs would have been allowed to enter the inter-LATA information services market – subject to the Section 272 safeguards – soon after adoption of the Telecommunications Act. Thereafter, local exchange competition might well have developed to the point at which the safeguards could have been eliminated by February 8, 2000.

Because Congress realized that there was significant uncertainty regarding the speed with which competition would develop, however, it gave the Commission identical authority to extend the sunset period for both inter-LATA telecommunications and information services safeguards. The proposed two-year extension simply adjusts the length of the sunset period to reflect the fact that BOC compliance with the market-opening obligations of Section 271 has taken far more time than Congress had anticipated.

Heightened non-discrimination obligation. The BOCs also fail to recognize that the Section 272 regime provides a unique safeguard: an absolute prohibition on discrimination that goes beyond that contained elsewhere in the Communications Act or the Commission's Computer Rules. Pursuant to Section 272, BOCs must treat all other entities in the same manner they treat their own Section 272 affiliates. The need to preserve this heightened non-discrimination requirement, standing alone, justifies extension of the sunset.

The BOCs' Reliance on *Computer III* is Misplaced

The BOCs' reliance on the Commission's *Computer III Orders* – in which the Commission held that structural separation is not necessary to prevent BOC anti-competitive abuse in the information services market – is misplaced. First, in the *California III* decision, the Ninth Circuit vacated the relevant portions of the Commission's *Computer III Orders*. Second, in adopting the Telecommunications Act, Congress rejected the Commission's finding that non-structural safeguards are an adequate substitute for structural separation. And, third, the Commission's recent *Bell Atlantic New York Section 271* Order recognizes the essential role of structural separation in preventing BOC anti-competitive abuse.

Threat of BOC Abuse in Inter-LATA Information Services Remains

Contrary to the BOCs' assertions, they retain the ability to cause competitive injury in the inter-LATA information services market.

- The BOCs' current small shares in the intra-LATA Internet access market does not prove that they lack economic power. As the BOCs have long argued, their role in this market is limited as a result of regulatory restrictions. Once the Commission lifts the inter-LATA services ban, the BOCs will be able to provide the full range of Internet services – including dial-up and broadband local transport services, the Internet gateway, the Internet backbone, and on-line content. As a result, the BOCs are likely to become far more significant participants in the information services market.

- The introduction of local broadband competition, as a result of the growth of cable modem service and data CLECs, does not demonstrate that the BOCs lack market power that they could use to impede competition in the inter-LATA information services market. More than ninety percent of all consumers still use traditional local exchange facilities – in which the BOCs retain a virtual monopoly – to access information services.

- The BOCs will continue to have market power when they are allowed to enter the inter-LATA market. As the Commission has observed, "In enacting Section 272, Congress recognized that the local exchange market will not be fully competitive immediately upon its opening."

- The fact that the inter-LATA market *currently* is competitive plainly is does not preclude BOC anti-competitive conduct. As long as they retain a significant degree of market power in the local exchange market, the BOCs will have the ability to favor their own information service operations – thereby distorting competition in the inter-LATA information services market.

Sunset of Section 272 Would Not Result in BOC Deployment of New Services

Finally, the BOCs fail to demonstrate that, if the Commission allows the Section 272 safeguards applicable to inter-LATA information services to sunset, they will deploy a new generation of innovative information services, which might not be economically feasible if the BOCs were required to offer them through a separate affiliate. The BOCs do not have a distinguished record as innovators – in information services or elsewhere. In any case, requiring

the BOCs to use a separate affiliate to provide inter-LATA information services will have no incremental cost because the BOCs will be obligated to establish a Section 272 separate affiliates to provide inter-LATA telecommunications services. The Commission has held that, once a BOC has set up that affiliate, the carrier may use this affiliate to provide inter-LATA information services.

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REPLY COMMENTS OF THE INFORMATION TECHNOLOGY ASSOCIATION OF AMERICA

The Information Technology Association of America ("ITAA") hereby replies to the comments filed by the Bell Operating Companies ("BOCs") opposing the Joint Request submitted by the Commercial Internet eXchange ("CIX") and ITAA. For the reasons set forth below, the Commission should grant the Joint Request and issue an order extending, until February 8, 2002, the date on which the Section 272 safeguards intended to accompany BOC entry into the inter-LATA information services market will sunset.

INTRODUCTION

The four surviving BOCs have filed strongly worded oppositions to the CIX/ITAA request to extend the sunset period applicable to BOC provision of inter-LATA information services. The BOCs, however, cannot compensate with rhetoric for what their submissions lack in reason. As demonstrated below, the BOCs have distorted the regime adopted by Congress –

recasting a carefully crafted regime designed to allow for BOC entry into inter-LATA markets while preventing anti-competitive abuse, into a meaningless set of provisions that would sunset before ever going into effect. They also place inappropriate reliance on the Commission's *Computer III Orders* – which have been vacated by the Court of Appeals, rejected by Congress, and undermined by the Commission's recent decision in the *Bell Atlantic New York Section 271 Order*. In addition, the BOCs have offered up a hodge-podge of irrelevant arguments to support their claim that they lack the ability to use their significant remaining market power to harm competition in the inter-LATA information services market. Finally, the BOCs make the wholly unsupported claim that, if the Commission allows the pro-competitive regime adopted by Congress to sunset, they will deploy a new generation of innovative information services.

I. THE BOCs HAVE FUNDAMENTALLY DISTORTED THE REGIME ADOPTED BY CONGRESS

In the Joint Request, CIX and ITAA demonstrated that Congress adopted a three-part strategy governing BOC entry into the inter-LATA telecommunications and information services markets.

- First, Congress barred the BOCs from providing in-region inter-LATA telecommunications and information services until they satisfy the "competitive checklist" designed to open local telecommunications markets to competition.

- Second, because the BOCs will retain significant market power even after they satisfy the competitive checklist, Congress provided that the BOCs initially will be required to provide in-region, inter-LATA services subject to pro-competitive safeguards. These include establishment of a separate affiliate, compliance with an absolute prohibition on discrimination that goes beyond the prohibition contained elsewhere in the Communications Act or in the Commission's Rules, and other behavioral safeguards.

- Third, Congress determined that, once the BOCs' market power is significantly reduced as a result of the growth of local exchange competition, structural and behavioral safeguards will no longer be necessary. While Congress anticipated that competition would develop rapidly enough to allow elimination of these requirements within a few years, it recognized that these critical competitive protections should not be eliminated prematurely. Congress therefore gave the Commission express statutory authority to extend the date on which the pro-competitive regime applicable to BOC participation in the inter-LATA telecommunications and information services markets will sunset for as long as the Commission deems necessary.[1]

In their replies, the BOCs have fundamentally distorted the regime adopted by Congress. As demonstrated below, the BOCs: (1) wrongly contend that Congress strictly limited the Commission's authority to extend the sunset period; (2) implausibly argue that, while Congress created a safeguards regime applicable to BOC provision of inter-LATA information services, Congress did not care in the least whether this regime actually is implemented; and (3) fail to recognize that the regulatory regime crafted by Congress imposes a non-discrimination obligation on the BOCs that goes beyond that contained elsewhere in the Communications Act or the Commission's Rules.

A. Congress Did Not Restrict the Commission's Authority to Extend the Sunset Period

At the outset, the Commission must determine the extent of its legal authority to extend the date on which the statutory safeguards applicable to BOC provision of inter-LATA information services will sunset. The two BOCs that address this issue – SBC and U S West –

[1] Request for Extension of the Sunset Date of the Structural, Non-Discrimination, and Other Behavioral Safeguards Governing Bell Operating Company Provision of In-Region, Inter-LATA Information Services, CC Docket 96-149, at 4-7 (Nov. 29, 1999) ("Joint Request").

assert that the Commission's discretion to extend the sunset period is "limited."[2] The Commission, they contend, may only do so if it demonstrates "unanticipated circumstances"[3] or marshals "compelling proof that the public interest would be harmed, absent an extension."[4]

SBC and U S West cite nothing in Section 272 that supports these assertions. The reason, of course, is obvious: Section 272 does not contain a single word that limits the Commission's authority. To the contrary, as CIX and ITAA demonstrated in the Joint Request,[5] the plain language of Section 272(f)(2) gives the Commission unfettered authority to "extend" the sunset period applicable to the safeguards governing BOC participation in inter-LATA markets "by rule or order."[6]

The Commission should be wary of any interpretation of the statute that would restrict its authority to extend the sunset applicable to the safeguards governing BOC provision of inter-LATA information services. Section 272 uses *identical* language in connection with the Commission's authority to extend the sunset date applicable to BOC provision of both inter-LATA telecommunications and inter-LATA information services.[7] Consequently, if the Commission were to adopt a restrictive interpretation of its authority to extend the safeguards in

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[2] Opposition of U S West Communications, Inc. at 4 (Dec. 17, 1999) ("US West Opposition").

[3] *Id.* at 3.

[4] Opposition of SBC Communications, Inc. at 3 (Dec. 17, 1999) ("SBC Opposition").

[5] Joint Request at 22.

[6] 47 U.S.C. § 272(f)(2).

[7] *Id.* at § 272(f)(1) & (2).

the current proceeding, it could inadvertently limit its authority to extend the effective period of the safeguards applicable to BOC provision of inter-LATA telecommunications services.

U S West's reliance on Sections 10 and 11 of the Communications Act, and Section 706 of the Telecommunications Act, is unavailing.[8] Contrary to U S West's suggestion, these provisions do not impose a limit on the Commission's rulemaking authority. Sections 10 and 11 establish the standard applicable to the Commission's review of existing regulations in response to a forbearance petition or as part of its Biennial Review. Section 706 plainly does not impose any independent constraint on the Commission's authority; it simply directs the agency to use its existing regulatory authority to promote the deployment of advanced services.[9] None of these provisions restricts the Commission's express statutory authority to extend the information services sunset period.

Nor is U S West's reliance on the Commission's Decision in the *Electronic Publishing Forbearance Order* justified.[10] To the contrary, that decision supports grant of the requested relief. In that proceeding, Ameritech asked the Commission to issue an order, pursuant to its Section 10 forbearance authority, to allow Ameritech to provide alarm monitoring services prior to February 8, 2001. The Commission declined. "In enacting section 275(a)," the agency explained:

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[8] *See* U S West Opposition at 4.

[9] U S West's position in this proceeding is the polar opposite of the position that it took in the *Advanced Services* proceeding – where it argued that Section 706 *expanded* the Commission's authority. *See Deployment of Wireline Services Offering Advanced Telecommunications Capability*, Memorandum Opinion and Order and Notice of Proposed Rulemaking, 13 FCC Rcd 24011, 24046 (1998) (*"Advanced Services Order"*).

[10] *See* U S West Opposition at 4.

> Congress made a policy judgment that the restrictions on [BOC provision of] alarm monitoring operations should sunset on February 8, 2001. Ameritech's petition is, in effect, a request that we adopt an earlier sunset date. Ameritech, however, does not contend that any changed or unanticipated circumstance warrants an earlier sunset. Instead, Ameritech recognizes that section 275 represents a legislative compromise, and essentially asks us to reopen and upset that compromise based on arguments Congress found unpersuasive in 1996.[11]

In the present case, as well, Congress has reached a "legislative compromise" – the BOCs are to be allowed into the information services market, but their entry is to be accompanied by a transitional regime of vigorous structural, non-discrimination, and behavioral safeguards. The BOCs are unable to cite any "changed or unanticipated circumstances" that would justify allowing them to enter the inter-LATA information market without *ever* complying with these safeguards. Indeed, the only "unanticipated circumstance" – the BOCs' failure to comply promptly with the market-opening provisions embodied in the Telecommunications Act – argues for extending the sunset period.

B. Congress Plainly Did Not Intend For the Information Services Safeguards to Sunset Without Ever Being Applied

The BOCs seek to make much of the fact that Congress provided that the Section 272 safeguards applicable to BOC provision of inter-LATA information services would sunset on a specific date, rather than expressly providing that the safeguards could not sunset until after the BOCs had begun to provide inter-LATA information services. "Congress," SBC asserts, "intended no tie between RBOC entry into interLATA markets and the sunset of the separation

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[11] *Petition of Ameritech Corporation for Forbearance from Enforcement of Section 275(a) of the Communications Act of 1934, as amended,* CC Docket No. 98-65, FCC 99-215, rel. Aug. 31, 1999, ¶ 8 (*"Electronic Publishing Forbearance Order"*).

requirements applied to in-region, interLATA information services."[12] Indeed, BellSouth goes so far as to claim that "Congress . . . was not concerned that continuation of the BOCs' alleged market power would create competitive problems in the interLATA information services market."[13]

The BOCs' position, apparently, is that Congress created the pro-competitive regime applicable to BOC entry into the inter-LATA markets, specifically applied this regime to both BOC provision of inter-LATA telecommunications and information services, but was absolutely indifferent as to whether the BOCs would actually have to comply with this regime at the time they are allowed to enter the market for inter-LATA information services. The Commission should be skeptical of any theory that suggests that Congress would act in such an irrational manner.

Congress clearly was concerned that the BOCs could use their significant market power to harm competition in both the inter-LATA telecommunications and information services market. Were it otherwise, Congress would not have adopted a comprehensive safeguards regime and applied it to *both* of these markets. Having adopted pro-competitive safeguards applicable to BOC entry into the inter-LATA information services market, Congress certainly must have expected that they would be implemented.

To be sure, because the Telecommunications Act provides that – absent Commission action – the application of the Section 272 regime to BOC-provided inter-LATA information services will sunset by February 8, 2000, it is *possible* for the Section 272 requirements

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[12] SBC Opposition at 4; *see also* Comments of Bell Atlantic at 3-4 ("Bell Atlantic Comments"); U S West Opposition at 3-5.

applicable to the BOCs' provision of inter-LATA information services to sunset before the BOCs are allowed to enter that market. By contrast, the application of the Section 272 regime to a BOC's provision of inter-LATA telecommunications services will not sunset until three years after the BOC enters that market.

The Conference Committee Report does not explain why the Congress selected February 8, 2000 as the sunset date for the information services safeguards. There is, however, a highly plausible explanation. The structure of the Telecommunications Act reflects Congress' desire to foster the rapid introduction of competition in the local exchange market.[14] Consistent with this objective, the most reasonable inference is that Congress simply assumed that most (if not all) of the BOCs would rapidly open their local markets to competition as required by Section 271.

Had the BOCs promptly complied with their regulatory obligations – as Congress intended and anticipated – they would have been allowed to enter the inter-LATA information services market soon after adoption of the Telecommunications Act. As a result, at the time of entry, they would have been subject to the Section 272 safeguards regime. Two years later, as provided by Section 272(d), the BOCs' compliance with the safeguards would have been subject to a rigorous audit.[15] Thereafter, local exchange competition might well have developed to the point at which the Section 272 safeguards could have been eliminated by February 8, 2000

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[13] Comments of BellSouth Corporation at 6 (Dec. 17, 1999) ("BellSouth Comments").

[14] For example, the Act provided that if no party seeks interconnection within ten months of the enactment, a BOC would be able to satisfy its market-opening obligation by filing a statement of generally available terms and conditions that complied with the Section 271 requirements. *See* 47 U.S.C. § 271(c)(1)(B). Once a BOC files an application to enter the inter-LATA markets, the FCC must act within ninety days. *See id.* at § 271(d)(3).

[15] *See id.* at § 272(d).

without any significant possibility that the BOCs could use their market power to cause anti-competitive injury in the inter-LATA information services market.

That, of course, is not what occurred. Rather, nearly 47 months after the adoption of the Telecommunications Act, the Commission has been able to find that only one BOC has brought itself into compliance in one of its states.[16] As a result, absent Commission action, the Section 272 safeguards applicable to inter-LATA information services will sunset before ever going into effect.

Congress' use of a more cautious sunset in the inter-LATA telecommunications market may simply reflect Congress' recognition of the differences between the inter-LATA information and telecommunications markets. At the time it adopted the Telecommunications Act, Congress was aware that – while both the inter-LATA information services and inter-LATA telecommunications markets were competitive – the level of competition in the unregulated, atomized inter-LATA information services market was even more robust than in the still-regulated, and somewhat more concentrated, inter-LATA telecommunications market. As a result, Congress could reasonably have concluded that it might be possible to eliminate the Section 272 requirements as applied to the inter-LATA information services market before doing so in the inter-LATA telecommunications market.

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[16] As the Commission just recently observed, "implementation of the congressional vision of increased telecommunications competition has, in many instances, not proceeded swiftly or smoothly." *Application of Bell Atlantic New York for Authorization Under Section 271 of the Communications Act to Provide In-Region, InterLATA Service in the State of New York*, Memorandum Opinion and Order, CC Docket No. 99-295, rel. Dec. 22, 1999, ¶ 4 (*"Bell Atlantic New York Section 271 Order"*), *appeals pending sub nom. AT&T v. FCC* and *Covad Communications Company v. FCC* (filed D.C. Circuit Dec. 28, 1999).

At the same time, however, Congress recognized that there was significant uncertainty regarding the speed with which competition would develop in the local telecommunications markets. As a result, as noted above, Congress gave the Commission authority to extend the application of the Section 272 regime in both the inter-LATA telecommunications and information services markets.

Consistent with congressional intent, the Commission should use its authority to extend the sunset of the inter-LATA information services safeguard for two years. Contrary to the BOCs' contention, this approach will preserve the distinction that Congress made between the sunset periods for application of the Section 272 safeguards to inter-LATA telecommunications and information services. The proposed two-year extension does not tie the sunset of the information service safeguards to BOC entry into the inter-LATA markets. Rather, it simply adjusts the length of the sunset period to reflect the fact that BOC compliance with the market-opening obligations of Section 271 has taken far more time than Congress had anticipated. Considering the extent of the BOCs' foot-dragging, such an adjustment is more than reasonable.

C. Congress Imposed a Heightened Non-Discrimination Obligation on the BOCs

The BOCs distort the regime adopted by Congress in an additional manner. The carriers assert that allowing the Section 272 safeguards to sunset will not reduce the protection against BOC discrimination in the provision of the network facilities and services that non-affiliated Information Service Providers need to provide their services.[17] This is plainly incorrect. In the *Non-Accounting Safeguards Order,* the Commission concluded that Section 272(c)(1)

[17] *See* Bell Atlantic Comments at 7; SBC Opposition at 12-13.

"impos[es] a flat prohibition against discrimination more stringent than the bar on 'unjust and unreasonable' discrimination contained in Section 202 of the Act."[18] Pursuant to this provision, the Commission explained, "the BOCs must treat all other entities in the same manner that they treat their section 272 affiliates."[19]

This obligation goes well beyond the BOCs' obligations, pursuant to the Commission's *Computer III* rules, to provide competing Information Service Providers with access to the BOC's network that is "comparable" – but not necessarily identical – to the access that a BOC provides its own information service operations. For example, under the Commission's *Computer III* rules, a BOC does not have to allow a non-affiliated ISP to physically collocate facilities used to provide information services – even if the BOC allows its own information service operations to do so.[20] Under the Section 272 safeguard, by contrast, the BOC would be obligated to allow non-discriminatory collocation.[21] The need to preserve this heightened non-discrimination obligation, standing alone, provides a sufficient basis for the Commission to extend the sunset.

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[18] *See Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended*, First Report and Order and Further Notice of Proposed Rulemaking, 11 FCC Rcd 21905, 21914 (1996) ("*Non-Accounting Safeguards Order*"), *petition for review pending sub nom. SBC Communications v. FCC*, No. 97-1118 (filed D.C. Cir. Mar. 6, 1997) (held in abeyance May 7, 1997), First Order on Reconsideration, 12 FCC Rcd 2297 (1997), Second Order on Reconsideration, 12 FCC Rcd 8653 (1997), *aff'd sub nom. Bell Atlantic Telephone Companies v. FCC*, 131 F.3d 1044 (D.C. Cir. 1997), Third Order on Reconsideration, CC Docket No. 96-149, FCC 99-242, rel. Oct. 1, 1999.

[19] *Id.*

[20] *See Amendment of Sections 64.702 of the Commission's Rules and Regulations (Third Computer Inquiry)*, Report and Order, 104 FCC 2d 958, 1038 (1986).

[21] *See Non-Accounting Safeguards Order*, 11 FCC Rcd at 22009.

II. THE BOCs' RELIANCE ON THE COMMISSION'S *COMPUTER III ORDERS* IS MISPLACED

The BOCs place heavy reliance on the Commission's *Computer III Orders* – in which the Commission abandoned the position, taken in the *First and Second Computer Inquiries*, that structural separation is necessary to prevent BOC anti-competitive abuse in the information services market.[22] The BOCs' reliance on these orders is misplaced for three reasons. First, in the *California III* decision, the Ninth Circuit vacated the relevant portions of the Commission's *Computer III Orders.* Second, in adopting the Telecommunications Act, Congress rejected the Commission's finding that non-structural safeguards are an adequate substitute for structural separation. And, third, the Commission's recent *Bell Atlantic New York Section 271 Order* recognizes the essential role of structural separation in preventing BOC anti-competitive abuse.

A. The Ninth Circuit Vacated the Commission's Finding That Non-Structural Safeguards are Adequate

Contrary to the BOCs' assumption, the *Computer III Orders* are not legally effective. In the Joint Request,[23] CIX and ITAA noted that the Ninth Circuit's decision in *California III* [24] struck down the portions of the *Computer III Orders* in which the Commission determined that non-structural safeguards are preferable to structural separation. As a result, CIX and ITAA pointed out, the starting point for the Commission's analysis must be the finding, in the

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[22] *See* Bell Atlantic Comments at 4-6; BellSouth Comments at 17-21; SBC Opposition at 12-14; U S West Opposition at 10-12.

[23] Joint Request at 19.

[24] *California v. FCC,* 39 F.3d 919 (9th Cir. 1994) (*"California III"*), *cert. denied,* 514 U.S. 1050 (1995).

Computer II Orders, that structural separation is necessary to prevent BOC anti-competitive abuse. This position is plainly correct.

In *California III*, the court held that "the FCC has failed to explain or justify its change in policy regarding nonstructural safeguards against access discrimination."[25] The court therefore concluded that the "cost benefit analysis" contained in the Commission's *Computer III Order*, which was intended to justify the elimination of structural separation, "is flawed and that portion of its order is arbitrary and capricious."[26] The court went on to specifically uphold only two specific portions of the *BOC Safeguards Order* – one dealing with BOC use of customer proprietary network information ("CPNI") and a second preempting the States from adopting certain regulations governing carrier participation in the enhanced services market – while vacating the remainder.[27]

The most reasonable construction of the court's decision is that it struck down the Commission's effort to replace structural separation with non-structural safeguards. The end-result was to return the industry to a *Computer II* structural separation regime – a fact recognized by the Commission when it granted the request, filed by the BOCs in the aftermath of the *California III* decision, for an interim waiver of the *Computer II* structural separation rules.[28] Therefore, the

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[25] *California III*, 39 F.3d at 933.

[26] *Id.* at 933.

[27] *See id.*

[28] *Bell Operating Companies Joint Petition for Waiver of Computer II Rules*, Memorandum Opinion and Order, 10 FCC Rcd 1724, 1730 (1995). U S West apparently continues to take this position. *See* U S West Opposition, Exhibit A, U S West Management Information Services, "Structural Separation of Enhanced Service Offerings, at 5 ("In overturning C-III, the [Ninth Circuit] re-instated the Computer Inquiry II (CI-II) rules, which require structural separation.").

starting point for the Commission's analysis of the Joint Request must be the agency's determination, in the *Second Computer Inquiry*, that only structural separation can effectively prevent BOC anti-competitive abuse in the information services market.

B. Congress Found That Structural Separation is Necessary to Prevent the BOCs From Using Their Market Power to Impede Competition in the Inter-LATA Information Services Market

Whatever the legal status of the *Computer III Orders* may be, the BOCs have failed to acknowledge a critical fact: When Congress adopted the Telecommunications Act, it was well aware of the Commission's conclusion, in the *Computer III Orders,* that non-structural safeguards are adequate to deter BOC anti-competitive abuse. Congress, however, plainly did not agree. Rather than directing the Commission to apply the *Computer III* rules to BOC participation in the inter-LATA information service market, Congress expressly provided that the BOCs were to provide these services subject to a comprehensive regime of structural, non-discrimination, and other behavioral safeguards.

Given the general deregulatory thrust of the Telecommunications Act, Congress' adoption of this regime clearly demonstrates its significant concern that the BOCs could harm competition in the critical information services market. The BOCs have not demonstrated any significant change during the last four years that justifies disregarding the clear policy choice made by the legislature.

C. The Commission's Recent Decisions in the *Bell Atlantic New York Section 271 Order* Recognized That BOC Compliance With the Section 272 Structural Separation Regime is of "Crucial Importance" in Preventing Anti-competitive Abuse

Finally, the BOCs' reliance on the *Computer III Orders* is misplaced because the Commission itself has come to recognize the need for structural separation to prevent BOC anti-

competitive abuse. In the *Bell Atlantic New York Section 271 Order*, released just last week, the Commission observed that the Section 272 separation requirements plays an essential role in preventing anti-competitive abuse. These requirements, the Commission observed:

> discourage and facilitate the detection of improper cost allocation and cross-subsidization between the BOC and its section 272 affiliate . . . [and] ensure that the BOCs do not discriminate in favor of their section 272 affiliates. . . . [C]ompliance with section 272 is "of *crucial importance*" because the structural, transaction, and nondiscrimination standards seek to ensure that the BOCs compete on a level playing field.[29]

Indeed, the Commission has recognized that structural separation is so effective a tool for preventing BOC anti-competitive abuse that it is desirable even in situations in which Congress has not expressly required its use. For example, the Telecommunications Act does not require the BOCs to provide advanced intra-LATA telecommunications services, such as digital subscriber loop ("DSL") services through a separate affiliate. Nonetheless, in the *Bell Atlantic New York Section 271 Order,* the Commission found that the establishment of a separate affiliate for the provision of advanced services would have significant pro-competitive benefits. As the Commission observed:

> Providing advanced services through a separate affiliate would reduce the ability of a BOC to discriminate against competing carriers with respect to xDSL services. Significantly, under this structure, the BOC would be required to treat rival providers of advanced services the same way that it treats its own separate affiliate. Because the BOC's advanced services affiliate would use the same processes as competitors to conduct such activities as ordering [DSL compatible] loops, and pay equivalent process for facilities and services, the creation of the [separate] affiliate should

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[29] *Bell Atlantic New York Section 271 Order*, at ¶¶ 401-02 (quoting *Ameritech Michigan Order*, 12 FCC Rcd 20543, 20725 (1997) (emphasis added).

> ensure a level playing field between the BOC and its advanced service competitors. We also believe that this structure would have the added benefit of increasing the availability and broadening the choices for advanced services for all Americans. A separate advanced services affiliate helps to attain the goal of encouraging entry into the provision of advanced services by numerous firms, in addition to the BOCs, while protecting against the risk that the BOCs could cripple these services in their infancy by discriminating against competing advanced services providers.[30]

The use of a separate affiliate to deter BOC anti-competitive abuse in the advanced services market, it must be noted, was proposed by Bell Atlantic itself – which told the Commission that "[e]stablishing a separate affiliate for xDSL services would ensure that competing providers of such services continue [sic] to receive non-discriminatory access to services and facilities."[31] Chairman Kennard has indicated that Bell Atlantic's decision to establish a separate advanced services affiliate was critical to his decision to support the grant of the carrier's Section 271 application.[32]

The information and advanced services markets have significant similarities: both involve provision of services that are "built on" underlying transport capacity providing by the BOCs and other incumbent local exchange carriers. The burden is on Bell Atlantic to explain why structural separation is a desirable tool to prevent BOC anti-competitive conduct in the advanced services market, but is unnecessary in the information services market.

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[30] *Id.* at ¶ 332.

[31] Letter from Thomas J. Tauke, Senior Vice President – Government Relations, Bell Atlantic, to Hon. William E. Kennard, Chairman, Federal Communications Commission, at 1 (Dec. 10, 1999).

[32] *See FCC Approves Bell Atlantic Long Distance Entry in N.Y.*, Communications Daily, Dec. 23, 1999.

Allowing the separate affiliate requirement applicable to BOC provision of advanced services to sunset would have a paradoxical effect. The Commission's policies plainly encourage the BOCs to provide stand-alone advanced services, such as DSL, through a separate affiliate.[33] However, absent Commission action, the BOCs are likely to take the position that they can provide a DSL-based end-to-end Internet access service – which is an inter-LATA information service – on an integrated basis. As the Joint Request makes clear, DSL-based Internet access services are in the early stages of development.[34] Absent the separate affiliate requirement, the BOCs may seek to "crush these services in their infancy" by providing their integrated inter-LATA information service operation with preferential access to the DSL-compatible loops necessary to provide a DSL-based Internet access service.

III. THE BOCs HAVE FAILED TO DEMONSTRATE THAT THERE IS NO LONGER A THREAT OF ANTI-COMPETITIVE ABUSE IN THE INTER-LATA INFORMATION SERVICES MARKET

The BOCs contend that application of the congressionally crafted safeguards to BOC participation in the inter-LATA information services market is unnecessary because they lack the ability to impede competition in the inter-LATA information services market. The BOCs marshal a hodge-podge of arguments to support this view. In particular, the BOCs insist that:

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[33] A BOC that seeks Section 271 approval to provide inter-LATA services, but that does not choose to provide advanced services through a separate affiliate, will be required to demonstrate "by the preponderance of the evidence that it provides DSL-compatible loops to competitors in a non-discriminatory manner." *Bell Atlantic New York Section 271 Order*, at ¶ 333. The Commission also has required the establishment of an advanced services affiliate as a condition of its approval of the applications filed in connection with the SBC/Ameritech merger. *See Ameritech Corp. and SBC Communications, Inc. Application for Consent to Transfer Control of Corporations Holding Commission Licenses and Lines Pursuant to Section 214 and 310(d) of the Communications Act and Parts 5, 22, 24, 25, 63, 90, 95 and 101 of the Commission's Rules*, Memorandum Opinion and Order, 14 FCC Rcd 14712, 14859-67, 14969-99 (1999).

[34] Joint Request at 12.

(1) the small share of the intra-LATA Internet access services market that their offerings have garnered demonstrates that they lack the ability to harm competition; (2) the growth of local broadband competition, from cable systems and CLECs, constrains the ability of the BOCs to act anti-competitively in the inter-LATA information services market; (3) by the time the BOCs are allowed to provide inter-LATA services, their market power in local exchange market will have dissipated to the point that they will lack the ability or incentive to harm competition in the inter-LATA information market; and (4) the current level of competition in the inter-LATA information services market prevents the BOCs from acting anti-competitively. None of these arguments is persuasive.

A. The BOCs' Current Small Market Shares in the Intra-LATA Internet Access Market Does Not Demonstrate That They Will be Unable to Act Anti-Competitively When They are Allowed to Enter the Inter-LATA Information Services Market

In their comments, each of the BOCs trumpets its failure to obtain a significant share of intra-LATA information services market – in which the BOCs have been allowed to participate for more than a decade. The BOCs focus on the market for intra-LATA Internet access service.[35] U S West, for example, notes that "BOC-affiliated ISPs have minimal market share."[36] Not to be out-done, Bell Atlantic announces that it "has been able to garner but 200,000 subscribers – less than two-tenths of one percent of the total market."[37] The BOCs' poor showings, they contend, demonstrates that they lack the economic ability to harm competition.

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[35] *See* Bell Atlantic Comments at 9-10; BellSouth Comments at 12-13; U S West Opposition at 6.

[36] U S West Opposition at 6.

[37] Bell Atlantic Comments at 9-10.

The BOCs' record in the intra-LATA Internet access market does not demonstrate that they will be unable to impede competition once they are allowed to enter the inter-LATA information services market. So long as the BOCs maintain monopoly control over the underlying transport facilities that rival ISPs require to provide their services, the BOCs will be able to engage in anti-competitive conduct. As the Commission has long recognized, unless constrained by an appropriate regulatory regime, a BOC can: use revenue from its non-competitive local exchange service to cross-subsidize competitive information service offerings; engage in a "price squeeze" by artificially inflating the costs of the underlying transport services that non-affiliated ISPs must use to provide service; and provide rival ISPs with inferior access to the transport services that they require.

The BOCs' suggestion that lack of economic power has prevented them from garnering a greater share of the information services market stands in stark contrast to their long-standing position that *regulatory restrictions* – especially the prohibition on BOC provision of inter-LATA services – have impeded them from being significant players in this market. Under existing rules, the BOCs' participation in the information services market is subject to very significant constraints. For example, a BOC cannot provide an end-to-end Internet access service. Rather, customers must obtain the inter-LATA component (which provides connectivity between a local point of presence and remote computer servers) by contracting with a so-called Global Service Provider. Similarly, the BOCs are not permitted to own Internet backbone

facilities. In the *Advanced Services* proceeding, the BOCs argued strenuously that elimination of these restrictions would enable them to deploy ubiquitous Internet services.[38]

Once the Commission lifts the restrictions on BOC provision of inter-LATA services, the BOCs will be able to provide the full range of Internet services – including dial-up and broadband local transport services, the Internet gateway, the Internet backbone, and on-line content. The Commission may even allow them to bundle these offerings with telecommunications services. As a result, the BOCs are likely to become far more significant participants in the information services market. ITAA has never objected to BOC participation in this market. However, ITAA has long argued that BOC participation must be accompanied by a regulatory regime that can effectively deter the BOCs from using their control over the local network to obtain an unfair competitive advantage in the information services market.

B. The Introduction of Competition in the Local Broadband Market Does Not Prevent the BOCs From Exercising Market Power

SBC and U S West claim that the growth of data CLECs and Internet-over-cable services prevents the BOCs from exercising market power in the market for high-speed local data transport services and, therefore, that the BOCs cannot leverage their position in this market to obtain an unfair competitive advantage in the market for inter-LATA information services.[39] ITAA has consistently supported Commission efforts to promote the growth of a competitive

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[38] *See, e.g., Advanced Services Order*, 13 FCC Rcd at 24044-48 (declining BOC request to eliminate restrictions that prevent the BOCs from providing Internet backbone services).

[39] *See* SBC Opposition at 7; U S West Opposition at 7 & 9. SBC contends that the Joint Request fails to show a "nexus" between BOC anti-competitive conduct in the market for high-speed local data transport services and competitive injury in the in-region inter-LATA information services market. SBC Opposition at 7. This is not a point that requires significant elaboration: To the extent that the BOCs have market power, they can use their

market for high-speed local data transport services. ITAA is confident that, over time, competitive local broadband services will be ubiquitous – thereby obviating the need for significant government regulation.[40]

The Commission, however, must be concerned with the marketplace as it exists today. The reality is that, at the present time, more than ninety percent of all consumers continue to access the Internet and other inter-LATA information services using ILEC-provided dial-up services. There is no question that, nearly four years after the adoption of the Telecommunications Act, the BOCs retain virtual monopolies in these markets. Until the BOCs' market power in the dial-up segment has been dissipated, the BOCs will retain the ability to harm competition in the adjacent inter-LATA information services market. Consequently, application of the pro-competitive safeguards crafted by Congress remains necessary.

C. The BOCs Will Retain Significant Market Power at the Time They Are Allowed to Enter the Inter-LATA Markets

SBC next contends that, because the BOCs "will not be able to provide in-region, interLATA information services until after the FCC finds that they have opened their [local exchange] markets to competition," there is no danger of BOC anti-competitive abuse because

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control over local transport facilities – whether conventional or advanced – to favor their own inter-LATA information services operations.

[40] The growth of data CLECs, however, will require the BOCs to comply with their obligations to provide the facilities that data CLECs require to provide services, such as DSL-compatible loops. To date, even Bell Atlantic – the one ILEC that has obtained Section 271 authorization – has failed to demonstrate that it is meeting its obligations to provide DSL-compatible loops. *See Bell Atlantic New York Section 271Order*, at ¶¶ 31-36 (finding that Bell Atlantic met its obligation to provide unbundled loops in the aggregate despite evidence that Bell Atlantic had failed to fulfill this obligation in connection with DSL-compatible loops.).

the BOCs "will have lost any perceived power they might otherwise have hoped to 'leverage' into interLATA information services markets."[41] This, of course, is plainly incorrect.

As the Commission has observed, "In enacting Section 272, Congress recognized that the local exchange market will not be fully competitive immediately upon its opening."[42] Congress concluded that the appropriate means to prevent the BOCs from using their residual market power in the local exchange market to impede competition in the inter-LATA markets is to require the BOCs to comply with a comprehensive safeguards regime. Although it has taken the BOCs far longer than Congress anticipated to open their local markets to competition, the underlying economic reality has not changed: At the time the BOCs are allowed to enter the inter-LATA information services market, they will retain a significant degree of market power. The Commission should ensure that, as Congress intended, the BOCs are subject to the comprehensive safeguard regime designed to deter the BOCs from using their market power to impede competition.

D. The Current Level of Competition in Inter-LATA Information Services Market Does Not Obviate the Need for the Statutory Safeguards

Finally, BellSouth asserts that because the inter-LATA information services market is *currently* competitive, there is no need to impose safeguards on the BOCs once they are allowed to enter.[43] BellSouth, of course, has gotten the matter backwards: Because the BOCs have not been allowed to enter the inter-LATA information services market, competition has taken root.

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[41] SBC Opposition at 6.

[42] *Non-Accounting Safeguards Order*, 11 FCC Rcd at 21911.

[43] *See* BellSouth Comments at 7-16.

Once the BOCs have opened their local markets, it will no longer be necessary to exclude them from adjacent competitive markets. However, as long as they retain a significant degree of market power in the local exchange market, the BOCs will have the ability to favor their own information service operations – thereby distorting competition in the inter-LATA information services market. Application of the Section 272 safeguards regime is necessary to deter the BOCs from doing so.

IV. THE BOCs HAVE FAILED TO DEMONSTRATE THAT ELIMINATION OF THE PRO-COMPETITIVE SECTION 272 SAFEGUARDS REGIME WOULD RESULT IN BOC DEPLOYMENT OF INNOVATIVE NEW INFORMATION SERVICES

The BOCs' final contention is that, if the Commission allows the Section 272 safeguards applicable to inter-LATA information services to sunset, they will deploy a new generation of innovative information services – which might not be economically feasible if the BOCs were required to offer them through a separate affiliate.[44] In support of this view, U S West has appended a study, commissioned in 1995, regarding the high cost, and deterrent effect, of structural separation.[45] These assertions are not persuasive for at least three reasons.

First, the BOCs do not have a distinguished record as innovators – in information services or elsewhere. ITAA is hard-pressed to understand why, if freed from the structural separation requirement, the very same BOCs who have been unable to obtain a significant share of the market for voicemail services can be expect to lead-the-way in deploying a new generation of innovative information services.

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[44] *See* Bell Atlantic Comments at 12; U S West Opposition at 3 & 11.

Second, the BOCs fail to account for the fact that, as a result of the Telecommunications Act, the costs of requiring structural separation for inter-LATA information services have fallen sharply. Pursuant to the Act, the BOC will be obligated to establish a Section 272 separate affiliate to provide inter-LATA telecommunications services. The Commission has held that, once a BOC has set up that affiliate, the carrier may use this affiliate to provide inter-LATA information services.[46] In effect, requiring the BOCs to use a separate affiliate to provide inter-LATA information services will have no incremental cost. Consequently, the BOCs can no longer persuasively argue that the cost of setting up a separate affiliate is likely to deter them from deploying inter-LATA information services.

Finally, both SBC and Bell Atlantic have concluded that they will have adequate economic incentives to provide advanced services even if they are required to do so through a structurally separate affiliate. These carriers have provided no basis to support their contention that it would be uneconomical to provide information services through a similar affiliate.

CONCLUSION

In adopting the Telecommunications Act, Congress struck a careful balance: it authorized the BOCs to enter the inter-LATA telecommunications and information services markets once they opened their local exchange markets to competition, but established a comprehensive safeguards regime designed to deter the BOCs from using their remaining market power to act anti-competitively. Congress anticipated that the BOCs would open their local

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[45] *See* U S West Opposition, Attachment A.

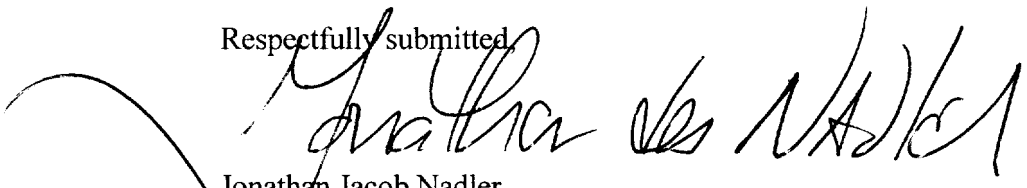
[46] *See Non-Accounting Safeguards Order,* 11 FCC Rcd at 21935.

markets quickly, and that the safeguards would soon become unnecessary. The BOCs, however, have not done so. Instead, they embarked on a four-year campaign intended to delay, dilute, and destroy the pro-competitive regime that Congress created.

If the Commission does not use its authority to extend the sunset date governing the application of the congressionally crafted safeguards to the BOCs' provision of inter-LATA information services, it will inadvertently reward the BOCs for their efforts. At the same time, the Commission will create an unnecessary risk of anti-competitive conduct in the information services market. The Commission should decline to do so.

For the foregoing reasons, as well as those presented in the Joint CIX/ITAA Request, the Commission should issue an order extending, until February 8, 2002, the date on which application of the Section 272 safeguards to BOC provision of inter-LATA information services will sunset.

Respectfully submitted,



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December 28, 1999

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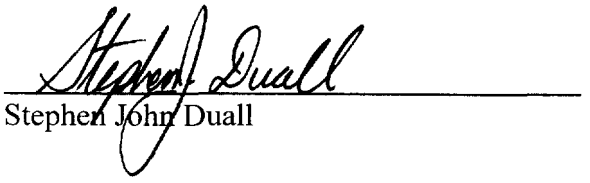

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